

**UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF MARYLAND
at Greenbelt**

In Re:	:	
Franklin Lamb	:	Case No. 96-1-1099-DK
	:	Chapter 7
Debtor.	:	
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Sebastian Corradino	:	
	:	
Movant,	:	
	:	
v.	:	Motion for Payment of
	:	Breakout Fee
	:	
Franklin Lamb	:	
	:	
Respondent.	:	

ORDER DENYING MOTION FOR PAYMENT OF BREAKOUT FEE

Before the court is a Motion for Payment of Breakout Fee (the “Breakout Motion”) submitted by Mr. Corradino, a former contract bidder for two properties located at 221 8th Street, N.E. and 328 9th Street, N.E., Washington, D.C. 20002 (the “Properties”). The Chapter 7 Trustee submitted a response supporting the reimbursement to Mr. Corradino of “reasonable and actual expenses incurred, excluding legal fees, in connection with his efforts to purchase the subject properties.” The court finds that the pleadings adequately set forth the parties’ arguments and that a hearing would not aid in the decisional process. For the reasons set forth herein, the movant’s Breakout Motion is denied.

Movant submitted an offer to purchase the subject properties, which were part of the debtor’s bankruptcy estate, for \$575,000.00. As required by 11 U.S.C. § 363(b), Trustee filed a Notice of Sale indicating his intention to sell the subject properties to movant. An objection to the Notice of Sale

was filed and a hearing was held. At the hearing, additional bids were submitted and the subject properties were ultimately sold to another purchaser for \$670,000.00. The parties assert that movant's offer to purchase the subject properties was the catalyst that resulted in other offers to purchase the properties and ultimately benefitted the estate. Movant now seeks reimbursements in the amount of \$9,902.20 for expenses incurred in connection with his efforts to purchase the subject properties. Specifically, movant requests the following reimbursements: \$1,826.00 in connection with general real estate expenses; \$2,511.20 for the formation of an ownership entity; \$2,500.00 for an appraisal conducted by Alliance Bank; and \$3,065.00 for consulting fees for financial, tax, and market analysis.

A breakout fee, also called a break-up fee, "is an incentive payment to a prospective purchaser with which a company fails to consummate a transaction." In re S.N.A. Nut Company, 186 B.R. 98, 101 (Bankr. N.D. Ill. 1995) (quoting In re Integrated Resources, Inc., 147 B.R. 650, 653 (S.D.N.Y. 1992)). "Agreements to provide breakup fees or reimbursement of fees and expenses are meant to compensate the potential acquirer who serves as a catalyst or 'stalking horse' which attracts more favorable offers." In re S.N.A. Nut Company, 186 B.R. at 101 (quoting In re Marrose Corp., 1992 WL 33848, *5 (Bankr. S.D.N.Y. 1992)). "Break up fees, where appropriate, should only be authorized where the fee is to compensate an unsuccessful acquirer which serves as the so-called 'stalking horse.'" In re Hupp Industries, Inc., 104 B.R. 191, 195 (Bankr.N.D.Ohio 1992).

In In re O'Brien Environmental Energy, Inc., 181 F.3d 527 (3d Cir. 1999), the Third Circuit Court of Appeals discussed the standards that should govern the award of breakup fees in the bankruptcy context. In that case, the Court rejected the business judgment rule as governing breakup

fees in bankruptcy and, instead, established that the determination of whether break-up fees or expenses should be allowed under 11 U.S.C. § 503(b) must be made in reference to general administrative expense jurisprudence. Id. at 535. “In other words, the allowability of break-up fees, like that of other administrative expenses, depends upon the requesting party’s ability to show that the fees were actually necessary to preserve the value of the estate.” Id. While breakup fees in corporate situations provide a prospective buyer with some assurance that it will be compensated for the time and expense incurred in putting together its offer if the transaction is not completed, the Third Circuit Court of Appeals recognized that not all of the purposes that breakup fees serve in corporate transactions are permissible in bankruptcy. Id. For instance, where a potential purchaser bids regardless of whether breakup fees are offered because the cost of acquiring the properties is less than the estimated value the purchaser expects to gain from acquiring the company, then the award of a breakup fee cannot be characterized as necessary to preserve the value of the estate. Id.

In In re S.N.A. Nut Company, the bankruptcy court articulated the same standard for evaluating a breakup fee that was later adopted by the Third Circuit. The test is whether the payment of a breakup fee is in the best interest of the estate; whether the interests of all concerned parties are best served by such a fee. In re S.N.A. Nut Company, 186 B.R. at 104. Bankruptcy courts should carefully scrutinize breakup fees to be sure that revenues will be maximized, and absent compelling circumstances that clearly indicate that payment of the fee would be in the best interests of the estate, breakup fees should not be awarded in bankruptcy. Id. at 105. Instead, the Court in In re S.N.A. Nut Company suggested that “the costs of bidding should be borne by those who are best able to bear them – the bidders who have voluntarily entered the bidding process, and who are bidding for a company (or

in this case, properties) with title free and clear of liens and with all the advantages provided by the Bankruptcy Code.” Id. at 106. The Court reasoned that due diligence costs are incurred for the benefit of the bidder, enabling that bidder to make an informed bid, and are not incurred for the benefit of the estate. Id.

If the reimbursement of costs is necessary to obtain the prospective purchaser’s bid and that bid results in a sale that benefits the estate beyond that which could have been otherwise obtained, a breakout fee may be justified. However, in the present case, a break up fee was not used, or needed, to induce movant to bid on the subject properties. No motion requesting a break out fee preceded the receipt of Mr. Corradino’s bid. Only after losing the bidding was a request for reimbursement made. Despite the possibility of an objection or of being outbid at a hearing, movant submitted a bid presumably because he realized that the potential value of the subject properties outweighed the cost of their acquisition. In other words, the expenses he incurred in the process of bidding were for his own benefit and cannot be characterized as necessary to preserve the value of the estate or as in the best interests of the estate. For these stated reasons, movant’s expenses are not reimbursable through an award of breakout fees.

Accordingly, it is, by the United States Bankruptcy Court for the District of Maryland,
ORDERED, that the debtor’s Motion for Payment of Breakout Fee is DENIED.

Date

DUNCAN W. KEIR
United States Bankruptcy Court
for the District of Maryland

cc: All Parties
All Counsel

Chapter 7 Trustee
Office of the United States Trustee